COMMERCIAL UNION ASSURANCE (MALAYSIA) SDN BHD

v.

PILIHAN MEGAH SDN BHD

HIGH COURT MALAYA, KUALA LUMPUR
AZMEL MAAMOR J
[ORIGINATING MOTION NO: R2-25-47-1998]
24 DECEMBER 1998

INSURANCE: *Contract of insurance - Extent of indemnity - Whether "consequential loss" can be claimed - Whether only losses which are pre-determined may be claimed - Whether concept of "forseeability" of loss or loss "resulting directly and naturally" does not apply to insurance law*

ARBITRATION: *Award - Setting aside - Principles applicable - When may an award be set aside, varied or remitted to arbitrator - Limitations to discretion to set aside award*

The applicant, an insurance company, agreed to indemnify the respondent under a Contractors All Risk policy ('the policy') in respect of loss or damage to insured property caused whilst contract works were carried out. As a result of massive landslips, parts of the main drains which were under construction collapsed. The drainage system was redesigned, realigned and constructed at a different location by the respondent. Consequently, a claim was made under the policy. Differences between the parties led to the matter being referred to arbitration.

The arbitrator allowed all three items claimed by the respondent. Being dissatisfied, the applicant applied to the High Court to set aside, vary or remit for reconsideration the last item allowed by the arbitrator. This last item was a claim for costs of constructing new drains at a new location. The applicant alleged that the arbitrator had made an error of law on the face of the award by allowing this item.

The policy had excluded any claim for consequential loss of any kind or description whatsoever. However, the arbitrator concluded that the said item was not a claim in respect of consequential loss but rather for loss resulting directly and naturally from having to construct the new drains.

The respondent contended that there was no error of law. It was further argued that even if there was an error of law, a specific question of law was referred to the arbitrator and as such no appeal lies in respect of the award.

Held:

[1] When one takes an insurance policy to cover his property against any form of risk it pre-supposes that the property must **exist** before or during the currency of the period of insurance. In the present case, construction of new drains at a different location was only made after the incident had taken place. It did not exist at the time when the incident happened. It is clear that such loss would undoubtedly come within the category of consequential loss but this has been expressly excluded under the policy.

[2] The arbitrator had made an error of law concerning the legal meaning of the words "consequential loss" using it in the context of a contractual or tortious claim, which is different from the understanding found in the insurance industry. In insurance contracts the extent of the risk assumed by the insurer is pre-determined. Therefore, the use of the concept of "**forseeability**" of the loss or loss "**resulting directly and naturally**" is wrong and unsustainable in insurance law as this is not a claim for a breach of contract or for a breach of tortious duty. This is a claim for **indemnity** under the insurance policy.

[2a] The last item was a consequential loss which was not anticipated or determined at the time of the signing of the insurance contract.

[3] This is not a case of the arbitrator committing errors of law in the course of determining a specific question of law expressly referred to him. No specific question of law was asked of him by any party nor was there mention of it in the arbitrator's award.

[Application allowed with costs.]

Case(s) referred to:

FR Absalom Limited v. Great Western (London) Garden Village Society Limited [1933] AC 395 ***(foll)***

Montgomery Jones & Co v. Liebenthal [1898] 78 LT 406 ***(foll)***

Ong Guan Teck v. Hijjas [1982] 1 CLJ 31 ***(foll)***

Sykt Pemborong Pertanian & Perumahan v. Federal Land Development Authority [1971] 2 MLJ 210 ***(foll)***

Theobald v. The Railway Passengers Assurance Co [1854] 10 Exh 45 ***(foll)***

Other source(s) referred to:

Insurance Contracts, Malcolm A Clarke, 2nd edn

For the applicant - Porres Royan (TJ Lee with him); M/s Shook Lin & Bok

For the respondent - K Rajendra (Miss Selvaratnam with him); M/s Azman Davidson & Co

Reported by Cindy Chan

JUDGMENT

Azmel Maamor J:

The applicant in this case applied by way of an originating motion for an order that part of the award of the arbitrator Y.M. Raja Aziz Addruse published on 1 April 1998 be set aside, varied or remitted for reconsideration by the aforesaid arbitrator.

The brief facts of the case are as follows. By a Contractors All Risk policy the applicant, an insurance company, agreed to indemnify the respondent in respect of loss or destruction or damage to Property Insured arising from any cause not otherwise specifically excluded by the policy. The policy was taken out in respect of contract works that were being carried out during the material times pertaining to a development project known as Bandar Puchong Jaya Project. The property that were covered under the policy were:

> the permanent and temporary works and the materials and all other things belonging to the respondent or for which he is responsible, brought on to the situation of the contract for the purposes of the contract and the contractors' plant, machinery and equipment whilst at the situation of contract, the property of the respondent as for which he is responsible.

The property was insured for the sum of RM2.4 million.

As a result of massive landslips on or about 20 December 1993 (which were preceded by heavy rainfall and flooding) at around kilometer 16 of the Kuala Lumpur-Puchong road, parts of the main drains which were under construction collapsed. The contract works that were involved at the time of the said incident were "the execution and completion of the main drainage system of Bandar Puchong Jaya."

As a result of the aforesaid incident, the the drainage system was redesigned, realigned and constructed at a different location by the respondent. By reason of the aforesaid the respondent alleged that it had suffered loss and damage and consequently a claim was made to the applicant under the policy for the following:

(a) the costs of drains and of materials damaged or rendered unsound due to the collapse. **RM552,839.76**

(b) the costs of drains not damaged but rendered unsuitable by reason of the order of the local authorities to relocate the drainage system. **RM469,929.13**

(c) the actual costs incurred in constructing the new drains at the new location. **RM7,147,883.43**

At the beginning the applicant only agreed to be liable under item (a) of the claim. Because of the existence of difference between the parties in the claim for items (b) and (c) the matter was referred to arbitration and both parties jointly agreed to appoint Y.M. Raja Aziz Addruse as a single arbitrator to adjudicate upon the said difference.

In the course of the proceedings before the arbitrator the applicant abandoned its defence of defective design of the drainage system. This means that the applicant no longer disputed liability. Hence the only issue to be determined by the arbitrator is the amount which the respondent was entitled to recover under the policy.

In this award dated 30 March 1998 the arbitrator allowed the respondent's claim in respect of items (a), (b) and (c). The applicant in this application was not challenging items (a) and (b) of the claim. It was only in respect of item (c) that the applicant alleged that the arbitrator had made errors of law on the face of the award where the arbitrator decided that the applicant was liable under the policy to pay to the respondent the costs of constructing the new drains at the new location amounting to RM7,147,883.443.

Hence the main issue that needs to be determined in this case is whether there was an error of law on the face of the award committed by the arbitrator in awarding damages to the respondent under item (c) of the claim. Counsel for the respondent strenuously argued that there was no error of law on the face of the award. He further argued that even if there was an error of law a specific question of law was referred to the arbitrator and as such no appeal lies in respect of the award.

It has been well established that in order for an award of the arbitrator to be set aside, varied or remitted for consideration by the court, there must exist one of the four grounds as held in the case of *Montgomery Jones & Co v. Liebenthal* [1898] 78 LT 406 where Chitty LJ said:

> I agree there are four grounds upon which the matter can be remitted to an arbitrator for reconsideration. Those grounds are (i) where the award is bad on the face of it (ii) where there has been a misconduct on the part of the arbitrator (iii) where there has been an admitted mistake and the arbitrator himself asks that the matter be remitted (iv) where additional evidence has been discovered after the making of the Award.

The principle of the above English case had been followed and applied locally in the case of *Ong Guan Teck v. Hijjas* [1982] 1 CLJ 31; [1982] 1 MLJ 105. Hashim Yeop Sani J (as he then was) held that:

> It has been settled law as early as 1898 in *Montgomery Jones & Co. v. Liebenthal & Co.* that the following grounds would constitute good grounds for the court to remit an award namely (i) where the award is bad on the face of it (ii) where there has been a misconduct on the part of the arbitrator (iii) where there has been an admitted mistake and the arbitrator himself asks that the matter be remitted (iv) where additional evidence has been discovered after the making of the award.

There are, however, limits for the court to exercise its discretion in setting aside an award of the arbitrator on the ground of error of law on the face of the award. One of the limits is clearly illustrated in the House of Lords case of *FR Absalom Limited v. Great Western (London) Garden Village Society Limited* [1933] AC 395 where Lord Warrington in his decision held:

> The question in the present appeal is whether the Award is bad by reason of error of law appearing on the face of it. This involves the further question, whether the question of law decided by the arbitrator was specifically referred to him for his decision or was only one which necessarily arose in applying ascertained facts to the terms of the contract.

Lord Warrington went on to say:

> I think it is clear that ... in order to come within the rule that a decision of an arbitrator on a point of law is final, it must be shown that the point is specifically referred. It recognises the distinction between cases in which a question of law is specifically referred for decision and those in which such a question is involved incidentally, as it is in the present case.

This decision of the House of Lords had been approved and applied locally (See *Syarikat Pemborong Pertanian & Perumahan v. Federal Land Development Authority* [1971] 2 MLJ 210.)

It is my intention to apply the principle as stated above in considering the application before me. The main issue that this court needs to determine is whether there was error of law on the face of the award committed by the arbitrator and if there was whether the question of law decided by the arbitrator was specifically referred to him for his decision. The counsel for the respondent had strenuously argued that the arbitrator had committed no error of law and even if he had done so the question of law decided by him was specifically referred to him.

The impugned part of the decision of the arbitrator is in respect of item (c) of the claim where the arbitrator held that the applicant was liable to pay for the cost of construction of the new drains, in the sum of RM7,147,883.43.

What the applicant/insurers agreed to indemnify the respondent/insured under the insurance policy was that:

> if during the Period of Insurance ... any part of the Property Insured shall be lost, destroyed or damaged as referred to in Section 1 hereof ... the Insurers will indemnify the Insured as provided hereunder.

The Property Insured is described as:

> The permanent and temporary works and the materials and all other things belonging to the Insured or for which he is responsible, brought on to the Situation of the Contract for the purposes of the Contract.

The errors of law alleged by the applicant that had been made by the arbitrator in the award are:

(1) the respondent is entitled to the cost of construction of the new drains; and

(2) Exception No. 9 of the policy does not apply.

In respect of the first error of law the arbitrator in his award had made the following legal findings:

(i) I cannot however accept the claimant's argument that the fact of the policy being an "all-risk" policy would necessarily entitle the claimant to be indemnified in respect of all the losses being claimed. The term "all-risks" defines the perils to be covered by the policy but cannot entitle the claimant to recover any loss (of whatever nature) which it may suffer from the peril (para 4.6(2) of the Award).

(ii) By the policy ... the property insured was "the permanent and temporary works and materials" involved in the construction of the main drains under the contract described as the "Bandar Puchong Jaya Project." The words emphasised necessarily imply that what is intended to be covered by the Policy is the works." (para 4.6(3) of the Award).

Yet, contrary to the above findings the arbitrator held that "the loss to the claimant is the cost of the construction of the new drains." I find it very difficult to see the logic of such finding of the arbitrator. When one takes an insurance policy to cover his property against any form of risk it pre-supposes that the property must **exist** before or during the currency of the period of insurance. In the present case construction of new drains at a different location was only made after the incident had taken place. It certainly did not exist at the time when the incident happened. It is clear to me that such loss would undoubtedly come within the category of consequential loss. But then the policy had excluded any claim for consequential loss of any kind or description whatsoever. Yet the arbitrator in his alternative holding in the award said:

> The Exception 9 does not apply as these are not claims in respect of consequential loss but are for loss resulting directly and naturally from the Claimant's having to construct the new drains. (para 4.8(1) of the Award)

In this respect I agree entirely with the submission of the counsel for the applicant that the arbitrator had made an error of law concerning the legal meaning of the words "consequential loss" using it in the context of a contractual or a tortious claim, which is different from the understanding found in the insurance industry. In insurance contracts the extent of the risk assumed by the applicant had been pre-determined. In this case the amount insured was determined at RM2.4 million being the original value of the contract to construct the said drains. Therefore the

use of the concept of "forseeability" of loss or loss "resulting directly and naturally" is wrong and unsustainable in insurance law. This is not a claim for a breach of contract or for a breach of tortious duty. This is a claim for **indemnity** under the insurance policy. Malcolm A Clarke in his book *Insurance Contracts* (2nd Edn.) said:

> So, whether an insurance contract covers consequential loss is a matter of the terms of the contract concerned. The insurance industry's notion of consequential loss is quite different from that of the lawyer.

And in the case *Theobald v. The Railway Passengers Assurance Co* [1854] 10 Exch. 45 Pollock CB said:

> What the insurance company calculate on indemnifying the party against is the expense and pain and loss immediately connected with the accident and not remote consequence that may follow according to the business or profession of the passenger.

The proper nature of claims that come within the meaning of "loss immediately connected with incident" and "consequently loss" is items (a) and (b) of the respondent's claim. In my view item (c) of the claim is consequential loss not anticipated or determined at the time of the signing of the insurance contract.

Based on the reasons as I have stated above I arrived at the conclusion that the arbitrator had committed errors of law when he held that the respondent was entitled to also claim item (c) of its claim. He committed these errors of law in the course of his arriving at the conclusion that the respondent was also entitled to item (c) of the claims as well. This is certainly not a case of the arbitrator committing errors of law in the course of determining a specific question of law expressly asked of him to make. I was unable to find any specific question of law asked of him by any party. No mention of it was made by the arbitrator in his award. I therefore ordered that that part of the award pertaining to item (c) be set aside.

In the circumstances I allowed this application with costs.